

THE COMMUNITY REINVESTMENT ACT OF 1977:

AN ANALYSIS OF APPLICATION CHALLENGES

by

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S.B., Massachusetts Institute of Technology
(1979)

SUBMITTED IN PARTIAL FULFILLMENT
OF THE REQUIREMENTS FOR THE
DEGREE OF

MASTER OF CITY PLANNING

at the

MASSACHUSETTS INSTITUTE OF TECHNOLOGY

June 1980

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Submitted to the Department of Urban Studies & Planning
on May 26, 1980 in partial fulfillment of the
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ABSTRACT

This thesis describes the legislative history of the Community Reinvestment Act of 1977, and the regulations promulgated by the Federal banking supervisory agencies. Nine applications by banks and their challenges by community groups are examined, one in detail. These cases show that community advocacy groups have an important role in enforcing the Act, although community group involvement is not always necessary. Negotiated settlements as well as challenges are possible under the CRA, and produce different results. The Federal agencies charged with implementing the Act appear to have different standards of enforcement. Finally, some of the possible prospects of the CRA are considered. Of these, the economic climate and electronic funds transfer would seem to have the greatest impact on the future of the CRA.

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ACKNOWLEDGEMENTS

Many thanks must go to my advisor, Rob Hollister, and my two readers, Larry Bacow and Jim Carras, for their time and thoughtful comments on this thesis. I appreciate their efforts, and wish them all well.

I also benefitted from the facilities and people at Massachusetts Urban Reinvestment Advisory Group, Inc.

My friend Deborah Cohen Shmueli gave me much encouragement, and I thank her.

Finally, all this would have been impossible without the financial and emotional support my parents gave their daughter when she decided to attend MIT. I was very fortunate.

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CHAPTER ONE

The lack of mortgage and other credit in a neighborhood is frequently pointed to as a factor contributing to neighborhood decline. Community activist groups accuse banks of refusing sound loans in certain poor, minority, or changing neighborhoods. This practice has been termed "redlining," and while banks may deny its existence, community groups maintain otherwise, and have lobbied for legislation forbidding it.

The Community Reinvestment Act of 1977 (CRA) was intended to address the redlining issue.¹ It declares that financial institutions have "a continuing and affirmative obligation to meet the credit needs of the local communities in which they are chartered,"² and requires the Federal agencies in charge of financial institutions to examine bank lending practices and records. Fulfillment of bank obligations, as reflected in their records, is determined by the agencies and is used as one of the criteria in decisions of whether to approve applications for bank acquisitions or expansions.

As the first year of the CRA's implementation ends, it is important to study how the Act has been used. How has it been implemented, and what have been the results? Because it is difficult to determine in general how banks may be adjusting their policies to comply with the CRA, this paper will examine closely the most visible aspect of the enforcement and compliance process: application challenges and their outcomes. These challenges demonstrate to all concerned how community groups use the CRA, and how Federal agencies have chosen to interpret the Act and banks respond to it. Thus these early application challenges have

helped to clarify the role and expectations of each actor, while also defining the scope of the Act and illustrating its limits.

This paper will examine several application challenges in an attempt to understand how the CRA is working. An analysis of the community complaints, bank responses, and regulatory agency decisions will do much to explain how the CRA is used, and will provide background for others' involvement with the CRA. It is not too early to begin, as well, to evaluate how effectively the CRA has worked to halt redlining.

I will begin the paper with a discussion of the Act itself: its legislative history, the regulations and their writing, and the assumptions and expectations about the CRA. This is done not only to be inclusive, but because the details of these matters can be important in any litigation.

Provisions of the Act

Acting in their finding of the banks' "continuing and affirmative obligation," the Congress in Section 804 of the Act indicates how it is to be fulfilled:

- ...the appropriate Federal supervisory agency shall--
- (1) assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of such institution; and
- (2) take such record into account in its evaluation of an application for a deposit facility by such institution.

The financial institutions covered by the CRA and their Federal supervisory agencies are:

Federal savings and loan associations, regulated by the Federal Home Loan Bank Board (FHLBB);

National banks, supervised by the Comptroller of the Currency (COC);

State-chartered trust companies that belong to the Federal Reserve System, regulated by the Federal Reserve Board (FRB); those that are federally-insured but not members of the FRS are regulated by the Federal Deposit Insurance Corporation (FDIC);

Savings banks (thrifts) that are insured by the FDIC are regulated by it as well.³

Applications that require consideration of CRA performance are those for permission to

- * open a branch office
- * relocate a home or branch office
- * acquire or merge with a regulated institution
- * receive Federal deposit insurance
- * become Federally-chartered.⁴

The reader should be aware of the gaps in coverage by the Act. State-chartered savings and loans that are not members of the Federal Savings and Loan Insurance Corp. (FSLIC) are not covered by the CRA; nor are non-FRS or -FDIC state banks or any credit unions. These kinds of financial institutions contain % of the nation's total deposits.⁵ Also, in the states which prohibit branch banking, only mergers and acquisitions are covered by the CRA.⁶

If this is all the Act says, why are the banks complaining of compliance burdens and community groups hailing it as a wonderful tool? Before discussing how the CRA is being used, we should examine what the Congress intended the Act to accomplish and how the regulations interpreted Congressional intent.

Legislative History

While the traditional focus of Federal banking regulation has been matters of bank "safety and soundness," the CRA is the latest in a series of laws passed by the Congress that subject credit extension to Federal oversight. The thrust of these new laws has been in the areas of consumer and civil rights, but even in these instances, the rationale for Federal involvement is couched in traditional values: the findings of the Congress in the Equal Credit Opportunity Act (ECOA) include the reasoning that "Economic stabilization would be enhanced and competition among various financial institutions...would be strengthened by an absence of discrimination..."⁷ Even after the fairly tough language contained in Sec. 302(a) of the Home Mortgage Disclosure Act (HMDA),

The Congress finds that some depository institutions have sometimes contributed to the decline of certain geographic areas by their failure pursuant to their chartering responsibilities to provide adequate home financing to qualified applicants on reasonable terms and conditions...

the Congress hastened to add that "nothing in this chapter is intended to...encourage unsound lending practices."⁸

These divergent perspectives are reflected in the CRA. While wishing to continue to push the banks to recognize and fulfill community credit needs, the Congress still maintained that such activities were to be "consistent with safe and sound operation."⁹

The CRA was introduced by Senator Proxmire (D-Wisc.) on 19 January 1977 as S.406--a bill "to encourage financial institutions to help meet the credit needs of the communities in which they are chartered, and for other purposes," (bill title). The original bill had the same findings and definitions as the final version, but also contained the concept

of Primary Savings Service Area (PSSA--defined as a contiguous and compact area where at least 50% of deposit customers reside),¹⁰ and related all bank reinvestment activity to it. Banks seeking deposit facilities were required to

- * demonstrate how credit needs were being met in current PSSA's, and
- * delineate the PSSA of the proposed branch; analyze how the bank planned to meet the credit needs of that area; and, indicate what proportion of deposits received in the new PSSA would be reinvested there.¹¹

Hearings on the bill were held before the Senate committee on Banking, Housing, and Urban Affairs (of which Proxmire is chairman) on 23-25 March 1977.¹² Ralph Nader, Gale Cincotta of National People's Action, the Massachusetts and Connecticut state banking commissioners, and some bankers testified in support of the bill, a few offering strengthening amendments.

The Federal banking regulatory agencies all expressed agreement with the goals of S.406, but declined to support it, citing possibly adverse consequences, or objecting as did Arthur Burns of the FRB, to the implication of credit allocation. (Credit allocation is the mandating of certain types or amounts of credit to certain areas, a practice which is strongly resisted by bankers.) Increased paperwork, statutory duplication of administrative discretion and the recently-enacted HMDA, and the separation of loan and deposit markets were all given as reasons by the banking trade organizations for their opposition to S.406.

In the end, the CRA was not approved as an independent bill. Indeed, it appears that it would not have passed had it not become a title of the 1977 Housing and Community Development Act. In the Senate

debate to delete the CRA provisions from the larger bill, Senator Morgan (D-N.C.) gave this account of the circumstances by which the CRA was added:

But during the markup of the housing bill (S.1523), which we are now considering, the Banking Committee voted to attach an amended version of S.406, the Community Reinvestment Act, to the housing bill.

I might add by way of emphasis that I did not have the privilege of being present at the time the housing bill was marked up, inasmuch as I was hospitalized at the time. However, I would add that later on, after I was able to return to the committee, we did reconsider the vote by which this section was added to the housing bill and by my recollection the vote was 7 to 7. Therefore, it being a tie, the motion failed and the section remained in the bill.¹³

The amended version to which Morgan referred contained several major changes.¹⁴ This version clarified the bill's intent to have the banking regulators, as part of their regular bank examination, assess a financial institution's record of meeting community credit needs. This decision to remove the original bill's reporting requirements and "piggyback" the CRA onto the regular examination procedures was a recognition that the reports would have been largely duplicative of the HMDA's. Reference to PSSA's was retained, but the banks were no longer required to submit information regarding proposed PSSA's in their deposit facility applications: rather, the banking regulators were to use their assessment of the institutions' records on meeting only current PSSA's credit needs as a factor in evaluating applications for deposit facilities. Also removed was a directive that Federal agencies "permit and encourage" community groups to testify at deposit application hearings.

The debate to delete the CRA from the housing bill focussed on the appearance of credit allocation and the anticipation of increased bank paperwork. Early in the debate, Morgan declared the bill was,

"...if not the first step toward the allocation of credit, or the requirement of allocation of credit by lending institution in America, it certainly was a foot in the door."¹⁵ Senator Sarbanes (D-Mary.) countered by stating:

There is nothing in this legislation that is going to require any lending institution to take any risks that are inconsistent with or contrary to the safe and sound operation of the institution..¹⁶ This legislation is extremely sensitive to that concern.

Proxmire pointed out that the conference committee had "deleted from the bill all reporting requirements. We said it would be necessary for regulatory bodies to rely on the information they already have..."¹⁷ The move to delete the CRA from the housing bill was defeated 31 to 40.

The final version of the Housing and Community Development Act, with the CRA as one of its titles, was approved in the Senate on 1 October 1977. The further changes in the CRA are explained in this exchange between Morgan and Proxmire:

Mr. Morgan:...Will the Senator explain to me the difference between the community (Re)Investment Act as we agreed to it earlier in the Senate and that which the conference committee agreed to?

Mr. Proxmire:...What this legislation does, in contrast to what passed, is to delay implementation for 390 days....It also redefines the primary service area to be served on a broader basis, so there is no question that it is not simply the immediate community where the bank is located. These are the two principal modifications.¹⁸

President Carter signed the Housing and Community Development Act of 1977, containing Title VIII--the Community Reinvestment Act of 1977-- into law on 12 October 1977.

Regulations

The banking regulatory agencies began to plan a set of joint hearings in preparation for implementation of the CRA, scheduled to begin in November, 1978. Included among the item on which the Agencies invited opinions were

- * how the terms "low- and moderate-income communities" and "credit needs", mentioned in the Act, were to be defined;
- * if community outlines were to be determined by political boundaries, such as city limits or SMSA's, or by economic considerations such as bank trading areas;
- * should the same CRA assessment standards be applied to all Federally-regulated financial institutions regardless of which supervisory agency is in charge or the size of the institution;
- * can an institution specialize in the type of credit it offers and, how is an institution's record to be assessed when it is just one of several institution in a community.¹⁹

Even though Senator Morgan proposed, and Senator Proxmire toyed with agreeing to, a deletion of Sec 806--the requirement for Federal banking regulatory agencies to draw up implementing regulations,²⁰ the above short list of question faced by the Agencies gives an indication of the issues raised by the wording of the Act.

The proposed regulations, released on 30 June 1978,²¹ indicated that the main thrust of the Agencies was to encourage communication between banks and members of the community about the need for, and availability of, credit:

The Agencies believe that it is more likely that community credit needs which can be met on a safe and sound basis will be met when members of the community are aware of the availability of credit, the lending institutions are well informed about community credit needs, and such institutions make a sincere effort to meet those needs.

Moreover, the Agencies stressed that they would not dictate how the institutions were to meet their CRA responsibilities:

The regulations...would not require institutions to offer particular kinds or amounts of credit...(the regulations) preserve to every institution the flexibility necessary to operate in a safe and sound manner, and to serve the convenience and needs of its community effectively and imaginatively.²²

The CRA Statement

As the means to force a financial institution to consider where it thought its "community" lay and what types of credit it was prepared to extend there, the proposed regulations required the adoption and annual review of a "CRA Statement" by the board of directors. The Statement, which would be available to the public, would include the institution's delineation of its community and credit services. Additional information the institution considered "helpful in describing how its efforts... relate to meeting types of credit needed by its community" could be included in the Statement.²³

The Agencies indicated that they would consider whether to exempt institutions located outside SMSA's with less than \$10 million in assets from the Statement requirement, but the solicitation for comments on the matter was prefaced by these words:

The Agencies believe that institutions are aware of the areas they serve and have well-articulated loan policies. The Agencies, therefore, believe that adoption of a CRA Statement would not be burdensome to institutions.²⁴

Two methods for determining a financial institution's entire community were outlined:

- a) using as boundaries those of the SMSA or county, with adjustments for geography or large size of area
- b) using the effective lending territory--that area around each office where a bank makes most of its loans and all equidistant points, with similar adjustments as in (a) permitted.

Besides these two methods, any other reasonable rule for outlining the entire community could be used by an institution. In any case, low- and moderate-income neighborhoods could not be gerrymandered out an institution's community, nor could the delineation be so general that it obscured the focus on local communities.²⁵

In addition to the community outline, the CRA Statement was to contain a list of specific types of credit it was prepared to make available in that community. In the general category of residential loans, for example, the Statement was to indicate the sub-categories "mortgages for 1 to 4 dwelling units" of "home improvement loans" if offered.

CRA Statements from the two most recent calendar years were to be kept in a public file, along with all CRA-related comments received by the financial institution during that time.

The final regulations did not allow any exemptions from the requirement for a CRA Statement. In addition, they prescribed the text of a public notice required to be posted in all bank lobbies. The notice stated that a CRA Statement could be obtained there, that comments on the financial institution's CRA Statement and performance could be sent to the appropriate federal supervisory agency or the institution, that the public comment file was available for inspection, and that individuals or groups could request notice from the supervisory agency of any applications filed by the institution with that agency.

Assessing the Record

As part of a regular bank examination, the Agencies would evaluate the institutions' record of helping to meet their entire communities' credit needs. The regulations required that the assessment be based on the CRA Statement and files as well as an institution's existing records such as its HMDA data. Twelve specific factors were given as those to be considered in assessing a financial institution's record (see appendix A). The first group of three refer to an institution's efforts to communicate with its community and incorporate the findings in its policies; the next four "deal with evidence of practices which are or may be in conflict with the purpose of the CRA," including violations of the ECOA, the examination of HMDA data, and the record of branch office openings, closings, and services. The branch office record can also indicate some of a financial institution's effort to meet the credit needs of its community, and the last group of factors includes examples of other activities that could reflect attempts to help meet credit needs: participation in local community development projects and the origination or purchase of certain community-oriented loans, including government-insured loans. Finally, the regulations include a recognition that the list is not exhaustive and that activities a financial institution may undertake may be limited by legal restrictions, size, economic conditions, and other restraints.

Because the list of assessment factors was not considered the only way financial institutions could respond to credit needs, the Agencies refused to devise a weighting scheme for those listed.

The final regulations repeatedly stressed the Agencies' "wish to encourage innovative responses to community needs and ... read(iness) to consider favorably any efforts to meet community credit needs."²⁷

Effect on Applications

Any deficiencies in CRA performance discovered during a routine bank examination can be pointed out by the Agency, which can then encourage the bank to improve. This, however, is not the chief enforcement mechanism of the Act. The Congress required an institution's CRA record of performance be considered when that institution seeks Agency approval of an application for a deposit facility,²⁸ and it is this application and approval process that drives the CRA.

Almost any financial institution may someday seek approval of a deposit facility application. Profits can be increased by doing a bigger volume of business, and one way to increase volume is to establish more branch offices or move present ones to more favorable locations. Another option might be to acquire or merge with other financial institutions: an institution feeling the pinch of high interest rates and increased competition may wish to be acquired by a more well-off concern. In all these instances, the CRA record of performance must be considered as the Federal banking agencies evaluate applications.

Each Agency has stated that it may use an institution's record of CRA performance as the basis for denying a deposit application. State-chartered institutions applying to receive Federal deposit insurance must submit a proposed CRA Statement, and the appropriate Federal agency would evaluate that, as well as consider the assessment of CRA performance

by the current state regulators.

The Agencies have retained the option of granting conditional approval to applications, as well as outright approval or denial. In any instance where the CRA record is a "material factor" in an Agency's deliberations, the Agency "will discuss the institution's record of performance in its statement announcing its decision."²⁹

Public Notice & Opportunity to be Heard

A major change in the regulations specifying the public's role in deposit facility application procedures was also a result of the CRA. Although not specifically required by the Act, the Federal banking regulatory agencies amended their existing public notice and application procedures in order "to provide greater public awareness of intended actions by banks to which the Community Reinvestment Act is applicable."³⁰

The revised regulations require financial institutions making deposit facility applications to publish notice of such applications in a general newspaper twice, instead of only once. Originally, the notice was required to be published only in the community in which the applicant proposed to do business; the new regulations require notice by publication in the following communities:

- * for branches, the communities of the proposed branch and the home office
- * for relocations of home or branch offices, the communities of the office to be closed, the office to be opened, and the home office
- * for charters and deposit insurance, the community of the home office or proposed home office
- * for acquisitions and mergers, the communities of each home office.

In addition, banks proposing to relocate must post notice of their applications in the lobby of the affected office.

Opportunities for interested persons to comment on applications were also clarified and expanded. The regulations allow anyone to comment on an application by writing to the Regional Director of the appropriate agency. Protests must be signalled by filing a written notice of intent to protest with the Regional Director within the required number of days after the last publication of the public notice. Those challenging an application may submit data, comments, and information in writing, and request a hearing on the application. All participants in a hearing have the right to make presentations as well as rebut others' presentations.

CHAPTER TWO

On 2 January 1980, the Massachusetts state banking commissioner denied an application by the Provident Institution for Savings in Boston to establish a branch in Newton. Because the denial was based on the Bank's failure to fulfill the aims of the state CRA, it is an important precedent. The Provident case gives an example of excellent work on the part of a challenging community group, and a thoughtful decision by the banking commissioner. It also illustrates some of the possible bank responses to a CRA challenge.¹

The Massachusetts state CRA is identical to the Federal version described earlier. The state banking commissioner, Gerald Mulligan, adopted the Federal CRA as an administrative policy on 21 February 1979. This move was initially viewed with some concern by anti-redlining groups, because it replaced a stricter reinvestment standard which the previous Dukakis-administration banking commissioner had established through her executive authority.

The application was challenged by the Massachusetts Urban Reinvestment Advisory Group (MURAG), which analyzed the Provident's history of extending credit in Boston neighborhoods, prepared testimony, solicited the support of local politicians and other community-based organizations, and involved the press.

The Provident is the oldest and largest savings bank in the Commonwealth. It has nearly \$1 billion in assets, six downtown offices, four neighborhood branches, and a branch in Saugus. The Bank had applied for permission to branch into Newton in the previous year (1978),

and had been turned down by then-Commissioner Carol Greenwald. Comr. Greenwald in her written decision indicated that the Provident's record of serving the credit needs of its community was "not impressive." She also cited the Provident's dearth of conventional mortgages and preponderance of FHA or VA mortgages in some Boston neighborhoods, the low level of community outreach, its low overall loan to asset ratio (54.4% as of 30 June 1978), and the non-representative composition of its board of trustees.

MURAG's Challenge

In general, it was MURAG's contention that the Provident should be aggressively and affirmatively ascertaining the credit needs of its community's low- and moderate-income areas, and then working to address those needs. Because of its size, an active role in participating in urban lending and community development projects should be expected, but the Provident had not acted.

MURAG used many of Greenwald's points as the basis of its challenge to the Provident's new branch application. Using HMDA data, they tabulated the number and type of loans made by the Provident in every Boston census tract in the year since its previous application. They testified at the 13 November 1979 public hearing that the Provident had given only 188 home mortgages--176 conventional, 12 government-insured--in the period July 1978 to June 1979 (fiscal 1979). Of the \$7,227,000 total value of those mortgages, they asserted that 35.9% was given as mortgages in the well-off Beacon Hill-Back Bay sections of the city. For the low- and moderate-income areas of Boston, MURAG cited these

figures for the same time period:

AREA	MORTGAGES	HOME IMPROVEMENT LOANS
East Boston	none	2
South Boston	4	2
Charlestown	8	none
Roxbury-Mission Hill	8	2

Even in the higher-income Dorchester neighborhoods of CedarGrove-Neponset, where the Provident had a branch office, there were no mortgages and only three home improvement loans.

The Provident had been cited in Greenwald's earlier denial as having "a clear continuing predominance of FHA/VA loans in certain inner-city neighborhoods." In the fiscal 1978 period she considered, the Provident made 246 home mortgages--168 conventional, 78 government-insured. In response to Greenwald's criticism, the Provident gave only 12 government-insured loans in the next twelve-month period. MURAG cited this drop as "clear evidence that the Bank has little understanding of the use of government-insured loans," but did not stress that the cutback in government-insured loans had not been made up for by an increase in conventional mortgages.

MURAG also attacked the Provident for its lack of community outreach efforts. It characterized the Bank's community participation as "isolated, one-shot efforts and not on-going commitments in helping meet local community credit needs." Nor, it claimed, did the Provident make an effort to ascertain the credit needs of low- and moderate-income communities or attempt to target their marketing to reach those areas.

Finally, MURAG pointed out that Provident's aggregate loan to asset

ratio of 54.4% (as of September 1979) was low when compared to other Boston savings banks. Securties made up 37.7% of its portfolio, indicating, MURAG claimed, "a lack of energetic involvement in mortgage lending."

Provident's Case

In its application and testimony, the Provident cited its heavy deposit outflow as the motivation to seek the more stable Newton deposits. It also pointed to its support of traditional community activities as edidence of its CRA performance. Later, they announced a bank reorganization that would improve their responsiveness to local credit needs.

The Provident stated that Newton residents had over \$52 million on deposit with it, and that establishing a branch in Newton would thereby serve public convenience. It also claimed that competition would be enhanced by their proposed branch, since over 90% of deposits held by all financial institutions in Newton Centre/Newton Highlands were held by only two financial institutions. Additionally, the Provident asserted that its presence in Newton Centre would keep that neighborhood shopping center viable.

Provident also stated that it sought the Newton branch as an opportunity "to obtain deposits apt to be more stable than some of the volatile deposits we have generated from the Suffolk County (Boston) Marketplace." As evidence of its need for such deposits, it claimed that Boston banks had experienced a heavy deposit outflow which had not occurred at the rest of Massachusetts banks: \$75 million in deposits were lost by the Provident in fiscal 1979. Even in the better times (1975-1977),

the Provident noted, deposits in Suffolk County grew only 3.15%, while Middlesex County banks (where Newton is located) had a 14.55% increase. As evidence of its lack of loanable funds, Provident cited its issuance of \$9 million worth of mortgage-backed bonds to compensate for decreased deposits.

The Bank also cited its work for the United Way, support of the Greater Boston Chamber of Commerce and Neighborhood Housing Services, and its speakers bureau as evidence of its involvement in CRA-related activities. Its assertion that it also met some of its communities' needs by sponsoring a girls softball team and a road race was mentioned in almost every news account of the hearing.

On the last day of the two-week period for public comment after the public hearing, the Provident submitted extensive supplemental material in support of their application. In his cover letter to the Commissioner, chairman and chief executive officer Garth Marston (a former FHLBB member who was just appointed by the Provident in March 1979) revealed a "major restructuring" of the Bank, the goal of which was "to make the Provident more responsive to the credit and other financial needs of the Community, including low- and moderate-income areas."

Items included in the reorganization were the establishment of a credit and loan division, the purpose of which would be to "enable the Bank to monitor lending activity more systematically and to formulate lending policies which are more responsive to the credit needs of its entire lending area." At the same time, branch managers would be given more authority in loan processing and in responding to local requests for financial assistance and expertise from community groups. The marketing division was also to be strengthened in order to "improve

the communication of the Bank's saving and lending services through advertising targeted to low- and moderate-income areas." In addition, the new post of director of public affairs was created, with responsibility to monitor all CRA activity and develop community outreach programs. Already completed, but not yet analyzed, was a survey of real estate brokers to discover ways the Bank could help prospective homebuyers. Finally, the creation of neighborhood advisory boards, made up of neighborhood representatives from all income levels, was announced.

The Provident also provided figures to rebut MURAG's loan numbers. The Bank used total number of loans and their dollar volume to make the following points: in fiscal 1979, the Bank wrote 429 new mortgages totalling \$27 million. While lending activity could be expected to decline because of the deposit outflows thrift institutions experienced, the Provident's lending activity in Boston declined only 18%, compared with a 58% decline outside the city. One-third of its residential mortgage portfolio represented properties in Boston. When its record of lending in Roxbury, South Boston, East Boston, Charlestown, and Dorchester was compared with that of four other big savings banks, the Provident characterized itself as comparing "very favorably."

Mulligan's Decision

On 2 January 1980, Comr. Mulligan announced his denial of Provident's branch application on CRA grounds. The denial was based solely on Provident's record of performance, for Mulligan had early in his decision found "the Newton Centre banking environment...capable of sustaining the proposed Branch office."

Mulligan noted that the CRA compliance examination "indicated unsatisfactory performance on most of the assessment factors."* Although examination reports are confidential, Mulligan chose several publically-known Provident policies to illustrate its "unsatisfactory performance:" its restrictive loan policies, its poor performance when compared with peer banks, and the Bank's lending record in communities where it had been allowed to branch. While Mulligan was impressed with MURAG's analysis (he was quoted as saying, "They are not amateurs,") he chose to discuss items not covered in MURAG's testimony.

First, he discussed Provident's restrictive loan application policies, which he termed had a "chilling effect" on would-be borrowers. He cited Provident's \$100 mortgage loan application fee as being among the highest of other large Boston savings banks surveyed; the non-refundable portion, \$50, was the highest among the surveyed banks. Examiners seeking applications at the Provident's ten branches found several branches with none and one branch insisting on an address for the mortgaged property before releasing an application form. Next, the Commissioner cited the Bank's refusal to consider any 10% downpayment mortgages as evidence of insensitivity to the credit needs of its low- and moderate-income population.

In another comparison of the Provident and peer banks, the Commissioner noted that Provident's 1-to-4 family conventional mortgage loans in the Boston SMSA as a percentage of total assets ranked the lowest of the four, "significantly lower than its three peers."

* Massachusetts has the same assessment factors as the Federal banking agencies. See Appendix A.

Finally, Mulligan discussed Provident's record of lending in a community after having opened a branch office in that community. In three of four instances, the Provident had less money lent out in mortgages after one year of branch operation than before the branch was established. "This pattern of disinvestment...compels a negative judgment with respect to (the Bank's) comment to serving the credit needs of its community."

The Commissioner took notice of Provident's reorganization plan and praised the real estate broker survey as one way to end the Bank's "apparent isolation from all levels of its community structure," encouraging the Provident to make "every effort to open channels of communication with the community" as necessary for any alteration of its lending practices. While the reorganization plan was judged not "concrete enough to warrant approval" after its poor record of CRA performance, the Commissioner indicated that should the Provident actually carry out the plan and the commitments contained in it, future applications could be approved.

Discussion

MURAG was instrumental in lining up opposition to the application in addition to preparing the substance of the challenge. Letters from US Senators Kennedy and Tsongas Boston City Councilman DiCara, Lt. Gov. O'Neil, St. Senators Brennan and Timilty and from community advocacy groups such as United South End/Lower Roxbury Community Development Corp. and Low Income Planning Aid were sent to the Commissioner's office urging denial. MURAG was also largely responsible for the press coverage,

which was mostly sympathetic.

MURAG took some risk in grounding its challenge in former Comr. Greenwald's previous denial. No one knew what to expect to expect from Comr. Mulligan, but as the banking commissioner in a new, pro-business administration, reference to Greenwald could have had an inflaming effect.

The quality of the Provident's preparation and testimony was very poor when compared to MURAG's. The newspaper coverage of the hearing must have been extremely embarrassing to the Bank. Why was the Provident so ill-prepared?

One reason could be that they just didn't know what to expect about CRA enforcement: the rules of branching applications had changed, and they weren't prepared. But this view overlooks the fact that the Provident had, only one year earlier, been sharply rebuked for its lending patterns by Greenwald in her denial of a Newton branch. The Provident didn't change as a result of that experience, and it is possible that they believed the new King-administration banking commissioner would be unlikely to demand improved performance or to turn their application down.

Gerald Mulligan was an unknown factor when the application and challenge were filed. He was assumed to reflect the pro-business orientation of Governor King, either because he shared it, or would be pressured into conforming with it. So why did Mulligan act as he did in denying the application?

MURAG's impressive challenge and their effective use of outside pressure created a difficult atmosphere in which to improve the application, even if Mulligan had personally wanted to. But in denying the application, Mulligan very carefully presented his own arguments for denial:

there was no discussion of any of MURAG's points in the Mulligan decision. Instead, he cited Provident's loan application policies and his own analysis of the neighborhood branch performance as reasons for denial. Thus, he astutely demonstrated his independence from the Governor and pressuring community groups.

CHAPTER THREE

This chapter describes eight more CRA-related cases and their outcomes so that the reader may get a more complete picture than only the Provident challenge would provide of how the CRA works. The material for these cases came from regulatory agency documents, community group newsletters, and in large part, from newspaper accounts. The cases illustrate two of the kinds of applications covered under the CRA, some of the methods of the Federal regulators charged with implementing and enforcing the Act, the range of decisions those regulators can take on applications, and the role of anti-redlining groups from across the country in challenging applications and negotiating with banks.

Greater New York Savings Bank¹

The first CRA denial was issued 23 April 1979 by the FDIC on an application by the Greater New York Savings Bank (GNYSB) to establish a Manhattan branch. The decision on the Brooklyn-based bank's application was the first to be reached on a CRA-protested application by any Federal regulatory agency.

The application had been challenged by South Brooklyn Against Investment Discrimination (AID), which said that GNYSB had not met the credit needs of the residents in its existing Brooklyn service areas, that the Bank had "very stringent" lending terms, and that GNYSB had stifled mortgage originations in favor of secondary market investments.

In November 1977, the Bank had announced an affirmative action program for residential lending, in which it said it "accepts and sets as

a target goal the annual investment of \$25 million insound residential mortgage loans in New York City." It had also agreed with AID and another community group to set as a target \$2.5 million in mortgage and home improvement loans for two Brooklyn neighborhoods, and to spend \$40,000 in those neighborhoods advertising mortgage availability.

On 5 September 1978, the New York State banking board approved the application, and GNYSB went on to seek FDIC approval.* FDIC hearings were held in October (to put this in perspective, recall that the final regulations were issued that same month). At its 10 January 1979 meeting, the FDIC made no decision, probably because there was some doubt and hesitation about granting a conditional approval, for fear of having the conditions termed credit allocation.

Shortly after the 10 January no-action meeting, the Bank made the following policy changes:

- * reopened mortgage lending to non-depositors
- * reduced the downpayment on 5-8 family residential mortgages from 50% to 25 and 35%
- * doubled the maximum size of FHA home improvement loans to \$15,000
- * increased the maximum for all loans to \$100,000 from \$75,000
- * began to advertise the availability of mortgage loans, installed a "Mortgage Action Phone" in the Bank lobby, and published a description of its lending policy and terms.

On 23 April, approximately one year after the application was filed, the FDIC met and denied it. The vote was 2 to 1, with the COC member favoring approval. In the majority decision, the FDIC noted that GNYSB had taken a series of positive steps, including advertising, contacts with real

* See the discussion of savings banks in Chapter 4.

estate brokers, and meeting with community groups. It also found that the Bank's current lending terms, despite AID's contention, were generally competitive with other Brooklyn banks. But the CRA record was "not sufficiently favorable" to permit approval, because "the percentage of the Bank's current flow of funds which is being committed to mortgages in the Brooklyn area, though increasing, remains at a fairly low level."

Bank of Indiana²

The second denial of an application on CRA grounds was announced by the Comptroller of the Currency on 2 November 1979. This case is important because the application was not formally challenged; the bank examination process had extremely important role; and because the actions and decision by the COC appear to set down one rule regarding policy shifts by banks making applications.

The bank involved was the Bank of Indiana in Gary. The application was for permission to merge the Bank with a shell bank corporation for the sole purpose of allowing Money Management Corp. of Chicago to acquire the 0.7% of Bank of Indiana shares it did not already own. This may seem confusing, but it is very important. Technically, even though the application was to combine an existing bank with a corporate shell, it is considered a merger, and so it is subject to the provisions of the CRA. Because of the nature of this type of merger, there is no impact on competition, and so the decision could be based on CRA issued alone.

There was no formal challenge to the application: the COC had two years previously received a complaint by the Gary Human Rights Commission alleging discriminatory lending practices on the part of the Bank. The COC based its decision on its three bank examinations conducted between

November 1977 and March 1979.

The COC stated that "the Bank's CRA record raises serious concerns, and has been determined by this office to be less than satisfactory." Specifically, the COC found serious deficiencies in Bank performance on six of the twelve CRA assessment factors, no record of outstanding performance on the other factors, and no evidence of any circumstances that would "justify its failure to respond to credit needs in Gary, or to inform Gary neighborhoods of the Bank's credit services."

The COC found that the Bank's efforts to ascertain the credit needs and communicate with the residents of Gary's low- and moderate-income communities were "extremely limited." (Assessment factors a & b: see Appendix A)

The Bank had adopted 1 to 4 family mortgage terms that required 30% downpayments, high compensating balances, and interest rates two points above prevailing market rates. The Comptroller held that the effect of such terms was to discourage mortgage applications, particularly from low- and moderate-income persons (assessment factors d & i). The Bank's geographic distribution of credit extensions, applications, and denials indicated

a consistent disparity in credit availability between the city of Gary and its surrounding suburban communities.... In addition, for housing-related credit, there were dramatic disparities between low- and moderate-income census tracts and those with above-moderate household incomes. (assessment factor e)

Finally, the COC felt that the Bank's loan terms and underwriting criteria had a discriminatory effect on low- and moderate-income applicants (assessment factor f). It cited the minimum loan size requirement

for both commercial and residential loans, "excessively restrictive" credit rating requirements, and the 990 square foot minimum dwelling floor size for mortgages. It also cited a Bank history of uncorrected ECOA violations.

The bank dropped some of the objectionable policies after filing the application. It had also appointed a vice-president for Gary affairs; made a commitment to make \$10 million of credit available over the next five years to qualified downtown Gary-area borrowers, subject to the completion of a civic center complex and a US Steel office tower; and indicated a willingness to consider participating in Gary's housing rehabilitation program.

The promises were not enough. The COC pointed to the Bank's lack of "firm commitment" and its "excessive contingencies" as reason for its lack of confidence that the changes would result in a substantially-improved performance. The decision laid down the following guideline:

such recent improvements may be valid considerations if, and only if, they are of a significant magnitude, and have been in effect long enough to demonstrate that they are already strengthening the Bank's performance and should eventually result in a satisfactory performance level. It must be emphasized once again that token improvements or policy changes undertaken immediately prior to or during submission cannot be construed as constitution good-faith compliance with the spirit of CRA.

AmeriTrust³

After an Ohio law permitting branching by merger went into effect on 2 January 1979, the CleveTrust Corp. filed applications with the Federal Reserve Board to merge three of its affiliate banks into its lead bank, Cleveland Trust. These and related applications were challenged

by the Buckeye-Woodland Community Congress (BWCC), a Cleveland anti-redlining group.

BWCC charged Cleveland Trust (the name of the holding company and its anchor bank was subsequently changed to AmeriTrust) with discriminatory lending practices, and cited destruction of loan applications, refusal to permit persons to fill out applications, and rejection of credit-worthy applicants on the basis of race.

At a 27 December meeting of the FRB, the Board put off a decision on the applications, and in a letter to AmeriTrust expressed its concern "that AmeriTrust lending personnel may engage in practices that result in the discouragement of creditworthy applicants." The letter included a list of suggested changes the Bank could commit itself to in order to "assure the Board of improved performance in the future." The suggestions included:

- * make publically-available the Bank's loan policies, creditworthiness standards, and appraisal standards
- * implement a non-discrimination training program for lending personnel
- * establish a credit counselling program
- * keep a log of every loan inquiry by race, national origin, other social factors, and disposition
- * begin a public awareness program to inform the public about these and other policies and services

The response of the AmeriTrust chairman Brock Weir denied any discouragement of credit applications, but went on

to the extent that our past record gives the impression that any such policies exist, we wish to assure the Board of our intention to correct such situations and to enhance and develop training programs which will minimize their occurrences in the future.

Weir balked at the log suggestion, claiming that it would cost \$1.275 million a year and "would indeed constitute an undue and severe penalty" if other banks were not required to do so as well.

The log was later imposed by the FRB as a condition of its approval on 22 February 1980 of the AmeriTrust applications. The board imposed the log because it found AmeriTrust's prescreening practices to be "serious violations" of the ECOA. The FRB and its examiners found evidence of prescreening at AmeriTrust's main office and three of the seventeen branch offices sampled. Because of the evidence, the decision said, it was "impossible to conclude with certainty that AmeriTrust had not engaged in discouragement of applications from low- and moderate-income areas."

Two of the seven FRB members felt that the log requirement was "excessive" and lacked "sufficient supervisory value to justify the costs to AmeriTrust."

Landmark⁴

In the first agreement reached under a FRB policy established after the AmeriTrust protests, the Landmark Central Bank & Trust Company of Wellston, Missouri and a Wellston community group affiliated with the Association of Community Organizations for Reform Now (ACORN) negotiated a settlement that led to the withdrawal of the Wellston group's challenge. The group had protested an application by Landmark's holding company to acquire another bank.

The FRB began the negotiation and mediation policy in an effort to avoid the time-consuming special examination procedures required when

an application is protested. The FRB estimated that 2,600 man-hours were needed for its CRA exams in the AmeriTrust protests. The policy attempts to help clarify the contested issues and resolve misunderstandings among the parties.

The Bank agreed to:

- * provide funds to purchase and improve homes in the predominantly black Wellston
- * make FHA loans at $\frac{1}{2}$ of 1% less than the standard rate
- * establish new credit standards and loan terms that were more flexible and more appropriate to the Wellston community
- * hire a planning firm to prepare a redevelopment plan for Wellston
- * continue a job training program
- * contribute \$5,000 to aid re-establishment of the Wellston Chamber of Commerce
- * open its main office on Saturday mornings for a 90-day trial.

Michigan National Corp.⁵

In another challenge before the FRB, the Board in December 1979 approved the application by the Michigan National Corporation, a Bloomfield Hill bank holding company, to acquire five banks. The application had been protested by the Michigan Committee on Law and Housing. The Committee made the following charges regarding CRA performance of Michigan National's nine banks:

- * minimal efforts to communicate credit information
- * a poor lending record in Detroit low- and moderate-income communities
- * gerrymandering of nearby low- and moderate-income areas from the lending territory of one Detroit bank
- * failure to comply with the technical requirements of the CRA and HMDA

- * making more housing-related loans in all-white Detroit neighborhoods than in integrated ones

With regard to the last charge, the Committee stated that race seemed to "play a major role" in lending patterns, and claimed that lending fell drastically "as soon as census tracts reached only 1 or 2% black population." The Committee also stated that the nine subsidiaries made only 29 conventional mortgage loans in all Detroit area low- and moderate-income communities during 1976 to 1978.

In the 6 to 1 majority decision, the Board acknowledged that some of the subsidiaries did not comply with the procedural requirements of the CRA and HMDA, and went on to say

the Board views this noncompliance as a serious matters and expects Applicant to take steps to ensure full and continuing compliance with these requirements before consumation of these proposals.

The Board also found that "far less housing-related credit was offered in low- and moderate-income neighborhoods than in the rest of Detroit neighborhoods. While the Board attributed part of the disparity to lack of demand, it also blamed Michigan National's "failure to determine systmatically the credit needs of the Detroit area and the fact that its advertising has been deposit rather than credit oriented."

The gerrymandering charge appeared unfounded once the total lending, rather than only the housing-related pattern was considered, and no racial discrimination appeared to exist, either. And, despite the lack of housing-related credit in low- and moderate-income areas, the subsidiary banks did participate in Small Business Administration programs and hold bonds issued by the Michigan State Housing Development Authority.

Three meetings between the Committee and Michigan National took place as part of the FRB's policy to encourage negotiated settlements in challenged applications. No settlement was reached.

First National Boston Corp.

The challenge of the First National Boston's proposed acquisition of Southeastern Bank & Trust Co. of New Bedford is interesting because it comes from a competitor, the First National Bank of New Bedford. The FRB voted unanimously in February 1980 to allow the acquisition to proceed.

First National New Bedford had charged that First National Boston had an "utterly abysmal" lending record, and made five specific CRA-related charges against the Boston bank:

- * inadequate efforts to determine local credit needs
- * closing of branches in low- and moderate-income Boston neighborhoods
- * mortgage loans were only a small percentage of its total loans
- * the draining of subsidiary banks' reinvestment funds by requiring those banks to participate in First National Boston loans.

The brief stated that First National Boston's ability to draw on its subsidiaries' assets made it possible for local credit needs to be ignored in favor of First National Boston's larger customers.

The FRB dealt with each First National New Bedford accusation. It noted that the Boston bank had a community investment department and a CRA policy committee. The branch closings did not leave the communities without "an adequate source of credit or other banking services." The

outflow of funds due to subsidiary participation in First National Boston loans was compensated by capital funds coming from the Boston bank.

The Board noted that First National Boston's mortgage loan volume should increase since it had dropped its "depositors only" policy, and stated that the ratio of loans to deposits in certain areas was not of as much concern as evidence, which the Board found, of First National Boston sensitivity to credit needs in those areas. The only suggestion for improved First National Boston performance was for the Bank to seek out and meet with community groups.

New England Merchants

Another negotiated settlement took place in Boston, between New England Merchants National Bank and MURAG. The settlement was prospective in that no challenge had been filed, and as part of the agreement MURAG agreed not to challenge a merger between Merchants and another bank holding company.

The agreement called for Merchants to devote 25% of its conventional mortgage and home improvement funds to loans in Greater Boston low- and moderate-income areas. It was estimated that this would result in about 100 more loans per year on 1 to 4 family structures than were previously offered. Credit terms would not be affected by the agreement: one bank official said, "We did not sign an agreement that will combat inflation."

Merchants also agreed to set up a loan counselling program, to eliminate its \$25,000 home mortgage minimum, to pay interest on tax escrow accounts, and to emphasize small business loans.

The agreement also covered creditworthiness ratings, calling for

all income, including part-time and overtime, of a loan applicant and spouse to be considered effective gross income. For persons lacking a credit history, bill payment and employment records would be used to evaluate creditworthiness.

Finally, the contract provided for the monitoring by MURAG of Merchants' compliance, and called for the bank and community-based organizations to work together on projects.

Commerce Bancshares

The only court case so far involving a challenged application does not tell us much about how the courts will deal with the CRA. The case involved the appeal by the Missouri ACORN of the FRB's conditional approval of the merger of two Missouri bank holding companies. The US Court of Appeals for the District of Columbia upheld, in October 1979 and without comment, the FRB's action.

ACORN had charged that the Manchester Financial Corporation of St. Louis had failed to meet its affirmative obligation to fulfill the credit needs of the low- and moderate-income neighborhood in which its bank was located. Commerce Bancshares, which was acquiring Manchester Financial, made some general commitments as a condition to the merger:

- * encouragement of mortgage applications in a 64-block area of St. Louis
- * newspaper and other advertisements of credit services
- * a promise to keep experienced lending officers at the Manchester
- * a promise to continue meeting with community groups

ACORN wanted specific lending guidelines as a conditions for approval, including 5% downpayment secured mortgages and 10% downpayment unsecured

mortgages, all with 30-year maturities.

Because the CRA had been passed but not yet come into effect, the FRB based its 16 June 1978 decision on the Bank Holding Company Act, and stated that both bank holding companies met that Act's requirements. Furthermore, that Act did not permit the Board to dictate credit services or terms. ACORN filed suit on 12 September 1978, contending that the Board had illegally disregarded lending performance standards required under the CRA.

Summary

An analysis of these and other challenges yields the following points:

1. There have been only three denials of applications on CRA grounds. The banking agencies are much more likely to give conditional approval than to deny an application altogether, having overcome their initial hesitation to grant conditional approvals. This change of emphasis--from outright approval or denial to conditional approval--has done much to strengthen the Agencies' ability to encourage improved performance.
2. Conditions for approval imposed by the regulatory agencies have avoided any requirement for certain types of credit offering or credit terms because of their concern over having these requirements labelled "credit allocation." Conditions imposed have mostly been requirements to develop affirmative advertising and marketing programs, public disclosure of creditworthiness and underwriting standards, more meetings between bank officials and community groups, the elimination of non-credit-related loan terms (such as minimum amounts and customer-only rules), and the implementation of CRA-related personnel training programs.

3. Negotiated settlements, in contrast to agency-imposed conditions, have focussed on the provision of certain kinds and amounts of credit to specified areas. The New England Merchants' agreement is of this sort. The regulatory agencies refuse to endorse credit allocation agreements, but accept them as part of negotiated settlements leading to the withdrawal of challenges.

4. Several standards of judging an applicants performance have emerged. One is the comparison of the applicant's performance with that of peer banks'. This was done in the Greater New York and Provident cases. Another standard is the evaluation of the record of performance of the applicant only on the assessment factors, as was done most clearly in the Bank of Indiana and First National Boston challenges.

5. The banking regulatory authorities must balance the importance of CRA considerations with other factors involved in evaluating an application. The FRB appears willing to consider an applicants CRA record to be "only part of the convenience and needs aspect,"⁹ to be evaluated along with other factors such as competitive effects. The COC has reluctantly approved a branch it would have otherwise denied on CRA grounds because it felt that retaining the branch, which would have otherwise been closed, was in the public interest. There has been no indication that the FDIC and FHLBB would not take similar positions.

6. The banking authorities differ in their willingness to accept commitments to improved performance as sufficient to justify application approval. The FRB has noted that commitments can "outweigh adverse aspects in a CRA record,"¹⁰ while the FDIC in its Greater New York decision did not grant approval because the commitments had not yet

resulted in large enough performance improvements. The Provident and Bank of Indiana regulators fall somewhere between those two positions, maintaining that without some evidence that altered policies have to some degree already strengthened CRA performance, they could not rely on promises of improved CRA performance.

Of the Federal regulators, I expect the FRB to be unlikely to ever deny an application on CRA grounds. They have noted their belief that CRA performance must be considered along with other factors and their willingness to accept commitments to improve performance. They have been innovative in setting up a negotiation policy and offering staff as mediators. This desire not to deny applications is not necessarily an accommodation of the banking industry: securing CRA performance commitments may be an effective and quick means of CRA enforcement. The FRB requirement that AmeriTrust keep the loan inquiry log has demonstrated that the FRB is not adverse to imposing stringent conditions to its approvals.

The COC and FDIC have already demonstrated their willingness to use denials as well as conditional approvals. The FHLBB has issued conditional approvals, but has not seemed to rule out, as the FRB has, the possibility of denials.

7. Community groups have a variety of roles connected to the CRA. As advocates of neighborhood and community interests, they can be challengers and negotiators. Challenges get the most attention and serve to establish a group to be contended with. Community groups can be instrumental in

lining up opposition to applications and arranging press coverage, but challenges are time- and effort-consuming and require an application to have been filed. Negotiations allow the community group to extract commitments from banks that the Federal agencies would not seek, and can be conducted with almost any bank at any time. Finally, community groups can help match banks with community development and reinvestment projects that need assistance.

8. Not all challenges are brought by community groups. The First National Boston challenge was an example of a competitor bank using the CRA, and the Bank of Indiana denial is an instance of agency initiative.

9. Examiners play an important role in the CRA process. The COC denial of the Bank of Indiana was a result almost entirely of its examination findings. Exams substantiate or disprove challengers' allegations of poor performance. In the Provident case, "undercover" examiners discovered shortcomings in loan application availability.

10. Decisions on CRA-challenged applications are made by the Federal banking authorities at the national level. The Washington offices determine outcomes, not the regional administrators. This is an indication of how concerned the agencies are to show their good intentions with respect to CRA enforcement. After having opposed the CRA when it was being considered by Congress, they are now anxious to avoid charges of undermining it through low-priority and low-status implementation and enforcement.

CHAPTER FOUR

Several independent conditions could effect how often the CRA can be invoked by community groups and how widespread its influence will become. As I see them, there are four main areas of interest:

- * the Home Mortgage Disclosure Act extension
- * electronic facilities
- * mutual funds, especially money market funds
- * the response of financial institutions to economic and regulatory conditions.

The HMDA extension will determine community groups' access to data necessary for challenge preparation. In essence, the remaining three items are factors that will affect the shape and functioning of the banking community. There is a great deal of uncertainty about what the effects of these changes will be: some will strengthen, others erode, the utility of the CRA by community groups. It is important to understand what these changes will be, and what will be their differential impacts on CRA compliance.

Home Mortgage Disclosure Act

The immediate prospects of the CRA depend on the extension of HMDA now being considered by Congress. Because of Congress' and the Agencies' decision to use available data for monitoring CRA compliance, the HMDA material a bank must annually prepare becomes an important means by which bank examiners can evaluate CRA performance. The HMDA is even more important to community groups, for it provides them the data on lending patterns they need to check a financial institution's credit extension.

The HMDA expires in June, 1980. The Federal Reserve Board has recommended a three-year extension, while the other Agencies have supported making HMDA a permanent requirement. Community groups want a permanent HMDA and would like to see a broadening of its provisions to include the small and non-SMSA financial institutions now exempted from HMDA compliance.

CRA enforcement relies heavily on community groups' involvement, and they in turn rely on HMDA data to document their application challenges. Without an extension, would-be users of the CRA will have to rely on the few state and local disclosure laws for data on lending patterns. The alternative, when disclosure data is not available, of canvassing neighborhoods to discover "unmet need" is time-consuming and expensive. Disclosure data, particularly HMDA, is essential to the enforcement of the CRA.

Electronic Facilities

The term "electronic facilities" can refer to both automatic teller machines (ATM's) and electronic funds transfer (EFT). Off-premises ATM's currently exist, and are already regulated by the banking authorities. However, the federal regulators have differed in their interpretation of whether the CRA applies to ATM's.

The FDIC has ruled that after a bank has applied for and met the CRA review for an initial ATM, any subsequent units are exempt from review. Also, ATM's shared by more than one bank are considered to be branches only of the bank which owns the facility, so permission is not needed to share a facility.¹

The CRA has caused the FHLBB to change its policy regarding off-premises ATM's.² Previously, the FHLBB had not required public notice before the establishment of such facilities, but now it feels that the words "facility with the ability to accept deposits," contained in Sec. 803(3)(c) of the Act, include off-premises ATM's. Savings and loans now wishing to set up ATM's must go through the application and public notice process as if they were establishing branches.

The second aspect of electronic facilities is electronic funds transfer. As computer systems become larger and more reliable, EFT's cashless and checkless society becomes possible. Instead of the check validation machines now at stores, EFT will have a machine to send signals that will actually deduct the price of the purchased goods from the consumer's bank account and credit the same amount to the store's account. Already some banks offer pay-by-phone services which allow customers to phone their bill-paying transactions: this is essentially EFT, albeit on a small, voluntary scale.

EFT is that banking of the future. The result of EFT will be the extension of most banking services to any place equipped with a computer terminal. Banking will no longer be the geographically fixed act it now is for most consumers. The need for bank branches will be sharply decreased, as consumers need only to go to a bank to open an account or initiate a loan: this will result in a decrease of branch applications to which the CRA would apply. Indeed, whether the CRA applies to EFT at all is doubtful. Certainly, EFT will not become a reality without legislation from Congress and oversight by the banking regulators, but the "every supermarket a bank" EFT world will come swiftly once approved,

and the CRA's place in such a world must be considered by the Congress before that occurs.

So electronic facilities' effect on the CRA is uncertain. Uncertain in the near future because different financial institutions will be regulated differently when they wish to set up automatic teller machines. The long-term effect of electronic facilities on CRA will surely be that of electronic funds transfer, and no one knows how CRA considerations will be incorporated into planning for that sort of banking situation.

Money Market Funds

If a bank and a savings and loan where each asked to name its toughest competitor, neither would likely cite the other: instead, both would point to money market mutual funds. The assets of the money market funds have grown tremendously, largely with money that had been on deposit with the banks and savings and loans. It has been estimated that Massachusetts financial institutions, for example, lost \$1 billion in assets to the mutual funds in 1979.³ This siphoning off of bank and savings and loan assets leaves those institutions with less capital and flexibility to meet their community reinvestment obligations.

Though there has been some shift in the bank/money market fund balance, it is unlikely that any of those lost deposits will return to the banks. Despite the lessening of the prime rate and aggressive competition to serve smaller investors, banks are still handicapped by the nature of their liabilities and deposit interest rate ceilings. Even though the Depository Institutions Deregulation & Monetary Control Act of 1980 (the banking reform act, for short) phases out the interest

ceilings, it does so very slowly over a six-year time period. The average passbook saver will see only a $\frac{1}{4}$ of 1% interest rate increase by September 1981.

Perhaps money market funds would demur at any likening of their actions or responsibilities to those of banks, but their free checking and low initial investment make them look very much like regular bank accounts. Should they be obliged to fulfill any community credit needs? The banks and savings and loans certainly think so. Those institutions see themselves as struggling under the disadvantage of maximum interest rate ceilings and restrictions on the types of investments they are allowed to make, with the added responsibility of meeting community credit needs. Money market funds have no such restrictions, and in fact, feel required only to seek the highest possible return for their investors. They argue that the short-term nature of their investments does not allow for meeting longer-range community credit needs. "The funds seek temporary parking places for their investors' dollars," is how one mutual fund employee explained the situation.⁴

The banks are even more emphatic about the CRA duties of money market funds that apply for banking privileges. The Federal banking regulators have ruled that trust companies which do not "perform commercial or retail banking services...other than as an incident to their specialized operations..." are not covered by the CRA.⁵ The Massachusetts state banking commissioner has indicated that he believes the state CRA applies to one money market fund, Fidelity Management & Research Corporation, which is seeking a banking charter to complement its mutual funds' services. Fidelity disagreed, stating that it intended to offer fiduciary

trust services, adding traditional banking services only if requested to do so by its customers. While Fidelity has since agreed to file a proposed state CRA statement, they will not be required to do so under the federal CRA for federal deposit insurance.⁶

In summary, there are several areas where money market funds and the CRA converge. First banks and savings and loans are having a more difficult time meeting their CRA responsibilities as their depositors withdraw their money to invest in money market funds. Then there is the argument that money market funds are, in effect, unregulated banks, and should be obliged to meet community reinvestment needs. Finally, must any money market funds that might actually seek a banking charter be considered to be admitting its true banking nature and thus be required to fulfill CRA responsibilities?

Regulatory and Economic Conditions

Various financial institutions are being faced with regulatory constraints from which they seek relief. While these constraints are not directly related to CRA performance, actions taken by a financial institution can effect how its CRA record is evaluated. I am referring to financial institutions' opportunity to alter their legal status, and thereby switch their Federal banking supervisors. I will discuss two examples: state-chartered mutual savings banks seeking Federal charters, and banks dropping their Federal Reserve membership.

Mutual savings banks, until recently, could exist only in those seventeen states that chartered them. Most sought Federal deposit insurance and so were regulated by the FDIC as well as the state banking

authorities. State laws limiting the kinds of services the savings banks could offer and their freedom to branch are common. For example, New York State permits a savings bank to establish one branch a year. Should a savings bank wish to take advantage of a branching opportunity, it would have to seek permission from both the state and FDIC regulators. The banks could only complain about service restrictions and applications delays, but now they have an option. The Financial Institutions Regulatory Act of 1978 provides for Federal chartering of mutual savings banks by the FHLBB. Federal chartering would allow unlimited branching and one-stop regulation, since the FHLBB would both charter and provide deposit insurance. The Federal charter option has been enhanced by the recent passage of the banking reform act, with its provisions for new investment and trust powers for savings banks.

Several mutual savings banks have applied for Federal charters, among them the New York Bank for Savings, the fourth largest mutual in the US. No conversions have been approved yet, and it is not clear whether the mutuals are not just using the Federal chartering option as a means to force their state regulations to liberalize their savings bank laws.

The Federal Reserve Board's reserve requirement has been a major banking topic for the last year. The FRB makes its member banks keep on deposit with it a certain percentage of their assets. Because the FRS pays no interest on these accounts, the member banks felt they were losing earnings, and some began to drop their membership, thereby going from FRB to FDIC supervision. The bank debate has been silenced by the passage of the banking reform act, which requires all financial institutions, whether FRS members or not, to set up reserve accounts with the FRS.

There are probably more instances of financial institutions being able to switch Federal supervisory agencies. Even though the Agencies jointly issued the CRA regulations and examiner guidelines, differential interpretation and application of the CRA by the Agencies could induce financial institutions to include regulatory CRA enforcement into their decision-making.

The economic climate affects the number and type of CRA-covered applications that will be made. Requests to merge with or acquire another financial institution and to branch can be expected to be the bulk of the CRA-related applications. There are several ways current conditions can affect the rate of those applications.

The interest rate hike is making some financial institutions seek mergers as a way to increase deposits and lessen their portfolios' concentration of older, lower-interest loans. The banking reform act allows savings and loans and savings banks to offer checking accounts and investment and trust services. These changes give all financial institutions essentially the same banking powers, and requires all of them to seek customers in the same market. The increased competitive pressures will be too great for some financial institutions and they will have to be acquired by or merged into other institutions. There are even predictions of mergers between commercial banks and thrifts.⁷ The trend in banking will be toward larger financial institutions as the smaller, independent ones disappear.

There is not such a clear trend visible when discussing branching. Certainly mergers will result in more branch offices for the institution involved. Banking associations are lobbying for the repeal of state banking prohibitions or limitations, but there is some evidence that

banks may not be in a rush to take advantage of any changes.⁸ The high cost of establishing branches and the poor earnings outlook have been cited as reasons for the hesitation. Automatic teller machines may provide a cheaper alternative to branches and, as discussed, have a different application process in some instances.

Conclusion

Different time frames must be considered when discussing CRA prospects. The most immediate consideration is the HMDA extension. Without an extension, CRA enforcement through application challenges will be greatly set back.

For the near future, the financial condition of the banking industry is likely to lead to a flurry of mergers and acquisitions and mergers, giving CRA activists a lever with which to force CRA compliance. The money market funds can be expected, at the same time, to continue to attract investors away from the banks, leaving the banks and CRA advocates with less money to devote to community reinvestment. The 1980 banking reform act's phasing out of deposit rate controls over six years' time will not do much to help the banks with their deposit problems.

By the time electronic funds transfer becomes prevalent, few of the premises on which CRA enforcement depends will any longer exist: there will be little need for banks to establish branches, and most merger activity will already have been completed. Other strategies for community reinvestment will have to be developed.

Certainly, the CRA is and will continue to be, a powerful tool for community advocates now and for the next five or so years. The use of

the CRA can be strengthened for these groups by including credit unions in its coverage and making the examiners' reports public.

The CRA is a flexible tool as well. Community advocacy groups can use it to confront banks before regulators, or to provide a framework in which to negotiate with banks about meeting community credit needs. The emphasis of its users can go beyond the ill effects of redlining to efforts to achieve help for community economic development projects. Recognition must be made of the possibility of a shift, over time, in credit needs from urban to rural low- and moderate-income communities. CRA can be used to force financial institutions to reconsider their charity policies and priorities: an increasing number are likely to contribute money and expertise to community development ventures. Finally, while everyone working with the CRA realizes its potential for displacement, the issue has been infrequently addressed. How can neighborhood reinvestment and avoidance of displacement both be part of the CRA?*

In five to ten years after the enactment of the CRA in 1977, I believe it will be technically obsolete, largely because the banking industry as we know it will have changed so much. Banking regulatory and economic conditions will all serve to weaken the CRA, because the CRA as it is presently written will cover less and less of the decision environment. What will follow the CRA?

The cases and analysis have shown the CRA to be important and effective in promoting bank recognition of community credit needs and involvement in neighborhood reinvestment and development. This

* MURAG was involved in one project in which a bank donated technical assistance and waived costs in arranging financing to enable tenants to take over their building as a co-op, averting a conversion to condominiums.

effectiveness depends, however, on a set of banking conditions that cannot be expected to continue. Economic and technological changes, such as the advent of electronic funds transfer, will alter the banking industry. This could begin a new sequence of post-CRA Federal reinvestment legislation and regulation.

Alternatively, there may be no need for statutory follow-up to the CRA. The planning catchword for the Eighties seems to be "partnerships." Banks and community-based organizations could learn from their CRA experiences how to sit down and work together toward community reinvestment. Together the banks and community groups could utilize government programs or lobby for appropriate programs. This mutual understanding of the business and mission of banks and community groups can be one of the most lasting accomplishments of the CRA.

APPENDIX A

CRA ASSESSMENT FACTORS

- (a) Activities conducted by the bank to ascertain the credit needs of its community, including the extent of the bank's efforts to communicate with members of its community regarding the credit services being provided by the bank;
- (b) The extent of the bank's marketing and special credit-related programs to make members of the community aware of the credit services offered by the bank;
- (c) The extent of participation by the bank's board of directors in formulating the bank's policies and reviewing its performance with respect to the purposes of the Community Reinvestment Act;
- (d) Any practices intended to discourage applications for types of credit set forth in the bank's CRA Statement(s);
- (e) The geographic distribution of the bank's credit extensions, credit applications, and credit denials;
- (f) Evidence of prohibited discriminatory or other illegal credit practices;
- (g) The bank's record of opening and closing offices and providing services at offices;
- (h) The bank's participation, including investments, in local development and redevelopment projects or programs;
- (i) The bank's origination of residential mortgage loans, housing rehabilitation loans, home improvement loans, and small business or small farm loans within its community, or the purchase of such loans originated in its community;
- (j) The bank's participation in governmentally-insured, guarantee, or subsidized loan programs for housing, small business, or small farms;
- (k) The bank's ability to meet various community credit needs based on its financial condition and size, and legal impediments, local economic conditions and other factors; and,
- (l) Other factors that, in the Agencies judgment, reasonably bear upon the extent to which a bank is helping to meet the credit needs of its entire community.

APPENDIX B
TABLE OF CASES DISCUSSED

Bank	(Location)	Challenger	Agency	Application	Outcome
Provident	(Boston)	Mass. Urban Reinvestment (MURAG)	Mass. Banking Commissioner	branch	denied
Greater New York Savings Bank	(Brooklyn)	So. Brooklyn Against Investment (AID) Discrimination	FDIC	branch	denied
Bank of Indiana	(Gary)	none	COC	merger	denied
AmeriTrust	(Cleveland)	Buckeye-Woodland Community Congress	FRB	branch, merger	conditional approval
Landmark	(Wellston, Mo)	Assoc. of Community Organizations for Reform Now	FRB	merger	negotiated settlement
Michigan Nat'l	(Bloomfield Hills)	Michigan Committee on Law & Housing	FRB	merger	approved
New England Merchants	(Boston)	MURAG	none	none	prospective negotiated settlement
Commerce Bancshares	(Kansas City, Mo)	ACORN	FRB	merger	approved, upheld on appeal

FOOTNOTES

Chapter One

¹Community Reinvestment Act of 1977, 12 October 1977, P.L. 95-128,
12 U.S.C. 2901

²CRA: Section 802(a)(3)

³CRA: Section 803(1)

⁴CRA: Section 803(3)

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⁷Equal Credit Opportunity Act, 28 October 1974, P.L. 93-495,
15 U.S.C. 1691, Section 502

⁸Home Mortgage Disclosure Act, 31 December 1975, P.L. 94-200,
12 U.S.C. 2801

⁹CRA: Section 804(1)

¹⁰proposed bill Section 3 (4)

¹¹proposed bill Section 4 (1)

¹²Hearings by the Senate Banking, Housing and Urban Affairs Committee on
S.406, 23-25 March 1977.

¹³Congressional Record, 6 June 1977, p.S8953

¹⁴amended bill, Title 4 of S.1523, Congressional Record, 7 June 1977,
p. S9117

¹⁵Congressional Record, 6 June 1977, p. S8953

¹⁶Ibid., p. S8961

¹⁷Ibid., p. S8960

¹⁸Congressional Record, 1 October 1977, p. S16114

¹⁹43 Federal Register, 19 January 1978,

²⁰Congressional Record, 6 June 1977 p. S8960

²¹43 Federal Register 29918, 11 July 1978

²²Ibid.

²³Ibid., p. 29920

²⁴Ibid., p. 29918

²⁵Ibid.

²⁶⁴³ Federal Register 47144ff., 12 October 1978

²⁷Ibid., p. 47146

²⁸CRA: Section 804(2)

²⁹⁴³ Federal Register 47146 12 October 1978

³⁰Ibid., pp. 47157

Chapter Two

Material for this chapter came from the testimony submitted to the banking commissioner, the commissioner's decision, and the following newspaper accounts:

"Boston Mutual Faces New CRA Test," American Banker, 29 October 1979 p. 2

David Warsh, "Some stiff opposition to Provident's branch," Boston Globe, 14 November 1979 p. 37.

David Warsh, "Provident's New Branch for Newton: Round 2 begins today," Boston Globe, 13 November 1979, p. 25.

Kirk Scharfenberg, "Who should serve whom?" Boston Globe, 17 November 1979, p. 9.

"Mass Groups Hit Mutual Branch Bid," American Banker, 19 November 1979, p. 28.

David Warsh, "Provident to alter city loan program," Boston Globe, 29 November 1979, p. 39.

"CRA Keeps Mass Banking Chief Occupied," American Banker, 4 December 1979, p. 2.

"1st CRA Branch Denial by Any State Issued in Mass," American Banker, 7 January 1979, p. 3.

Chapter Three

- ¹This case is largely taken from: Keith Rolland, "Greater New York Wins Branch After Debate," American Banker, 6 September 1978, p. 1; K. Rolland, "FDIC Denies Greater NY CRA-Protested Branch Bid," Ibid., 25 April 1979, p. 1.
- ²Decision of the Comptroller of the Currency, 2 November 1979; "C of C Issues 1st CRA Denial, Bars Merger of Indiana Bank," American Banker, 30 November 1979, p. 1.
- ³"Buckeye-Woodland Dumps AmeriTrust in Fed's Lap," Disclosure, January, 1980, p. 4-5; "Society NB Agrees to Alter Lending," American Banker, 18 January 1980, p. 1; "AmeriTrust Told to Log Loan Queiries," Ibid., 25 February 1980, p. 1.
- ⁴"Mo. Bank, Local Bank Resolve Redlining Dispute under New Fed Negotiation Policy," American Banker, 13 November 1979, p. 1.
- ⁵"CRA Protest Set on Michigan Bid," American Banker, 23 August 1979, p. 14; "Fed Votes BHC Bid Despite CRA Protests," Ibid., 10 December 1979, p. 1.
- ⁶K. Rolland, "Agencies Weigh Stipulating Conditions For Granting Some CRA-Protested Plans," American Banker, 2 April 1979, p. 1; "Fed Votes Protested Mass. Aquisition," Ibid., 13 February 1980, p. 2.
- ⁷CRA Compliance Agreement between New England Merchants and MURAG, 22 February 1980; "Boston Bank Allots Up to 25% of Annual Mtge. Money for Lower-Income Areas," American Banker, 27 February 1980; Bruce Mohl, "Bank to reserve loans for low-income areas," Boston Globe, 23 February 1980, p. 1.
- ⁸Board of Governors, Federal Reserve System, Summary of Order, 16 June 1978; P. Battey, "Judges Hit Mo. Groups Challenge of Fed-Approved Merger," American Banker, 24 October 1979, p. 3; P. Battey, "Court Upholds Merger of Two Missouri BHC's Challenged Under CRA," Ibid., 7 November 1979, p. 1.
- ⁹Federal Reserve Board Information Bulletin, reprinted in American Banker 30 January 1980, p. 16.
- ¹⁰Ibid.

Chapter Four

- ¹John Yoch, "Plan to Exempt EFT from CRA is Argued in NY," American Banker, 31 January 1980, p. 3.
- ²43 Federal Register 47159 12 October 1978.
- ³"Mass Studies CRA Curb on Funds," American Banker, 22 April 1980, p. 1.
- ⁴Ibid.
- ⁵43 Federal Register 47155, 12 October 1978.
- ⁶"Big Money Fund to File CRA Plan," American Banker, 16 April 1980, p. 1.
- ⁷"A Bank Merger Policy of the 80's," American Banker, 7 April 1980, p. 4.
- ⁸"Economic Climate makes Ill. bankers Suprisingly Bearish on Bricks and Mortar," American Banker, 12 March 1980, p. 2.